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SUBJECT: KDDI WINS IN JAPAN'S MOBILE MARKET IN 2006, BUT 3-WAY OLIGOPOLY CONTINUES TO STIFLE COMPETITION

¶1. (SBU) SUMMARY: With music download services and handsets designed to appeal to the young, KDDI was the clear winner of the first round of competition since customers were allowed change mobile operators without having to change phone numbers starting in late October 2006. Nonetheless, the dowdy but still dominant NTT DoCoMo should be able to maintain its dominance as Japan's largest mobile carrier for several more years. The upstart Softbank, which had hoped to shake up the mobile phone market after buying out Vodafone in 2006, stopped Vodafone's losses, but was mired in self-made troubles over its ads and the inability of its systems to handle new orders. Japanese subscribers benefited from the heightened competition with rebates and new discount calling plans. The Communications Ministry (MIC) has set up several study groups to consider ways to bring more competition into Japan's mobile phone three-way oligopoly. End Summary.

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Everyone wins, but KDDI wins more than others
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¶2. (SBU) In 2006 all mobile phone operators gained subscribers, but KDDI outperformed its competitors by picking up more than two and a half million new subscribers. DoCoMo picked up less than two million subscribers for the first time in years. All three saw their stocks soar to record highs in early 2007, but, again, KDDI outpaced DoCoMo and Softbank with gains of over 40 per cent since the end of 2005, according to Nikkei figures.

¶3. (SBU) The market shares and number of subscribers of the three companies in early 2007 were: NTT DoCoMo 55% with about 52 million subscribers; KDDI almost 29% with over 27 million subscribers; and Softbank with only 16% and about 15 million subscribers. Nearly all KDDI subscribers use its more advanced and more expensive 3G service, while only about 60% of DoCoMo's subscribers and less than half of Softbank subscribers pay for 3G service.

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More focus on new services than on new subscribers
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¶4. (SBU) The increased competition afforded by number portability did not lead to a price war in the mobile phone market as some expected, but rather to new calling plans and fancier handsets. With subscribers reaching about 100 million, Japan's mobile market may be reaching the saturation point. Japan's mobile carriers realize that the best way to boost revenues now is by selling more content and services, such as music, videos, games, manga, and internet and

financial services. At this point, KDDI provides the most popular entertainment services, including Japan's most popular music download services. KDDI also began providing Google search at the top of its internet connection service last year, making it easier for users to navigate web pages on their mobile phones. Softbank's tie-up with Yahoo also provides its subscribers with a wealth of content.

¶5. (SBU) DoCoMo realizes it needs to attract more young subscribers and is cutting prices on its cell phones and on internet access, and providing more content aimed at the young, such as MTV videos. DoCoMo is still far ahead of the other mobile carriers in financial services, especially the "keitai saifu" or wallet phone which allows subscribers to use their DoCoMo phone as a credit card in over 70,000 retail stores.

GOJ looks at ways to increase competition

¶6. (SBU) Opening up Japan's mobile market with number portability is just one of the ways the Communications Ministry (MIC) has been trying to increase competition in the last couple of years. MIC opened the mobile market and offered some limited spectrum to a few new entrants in 2005, but the biggest of these, Softbank, opted instead to buy out Vodafone, the third largest mobile operator.

¶7. (SBU) When eMobile, the first new entrant in over a decade, starts service at the end of March 2007, it will not even try to compete for regular subscribers but instead focus on providing high-speed data services for businesses. Thus eMobile will largely be competing with another small carrier, Willcom, which also offers flat rates for data transmission.

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¶8. (SBU) One Communications Ministry study group is now looking at how it can change the structure of Japan's mobile phone market in which the three main carriers control everything from handset design to marketing. In addition, the Ministry recently introduced new guidelines which would permit new entrants by Mobile Virtual Network Operators (MVNOs). (Note: A Mobile Virtual Network Operator is a company that does not own its own spectrum or network infrastructure but resells wireless services under its own brand name, such as Disney or MTV.)

¶9. (SBU) MIC is also studying other obstacles that discourage consumers from changing carriers, including certain sales incentives and Subscriber Identity Module (SIM) locks. Japan's mobile phone manufacturers currently produce handsets that can only be used with one mobile carrier and prevent consumers with SIM locks from transferring SIM cards to the handset of another carrier. (In theory, the SIM card should allow users to change phones easily by removing the SIM card and inserting it into another mobile phone, thereby eliminating the need for activation of the new mobile phone on the network.)

Comment:

¶10. (SBU) Number portability did provide a boost for KDDI and increased competition in Japan's mobile market, but only among the established members of the oligopoly. The Communications Ministry realizes that Japan's mobile carriers and manufacturers need to open up to more competition or they may be doomed to become rather minor players within the global market. Tokyo-based U.S. observers of Japan's telecoms market believe that only by opening up the structure of the domestic market will Japan's telecoms carriers and manufacturers be able develop and compete overseas. However, Japan's mobile carriers and manufacturers, who work hand-in-hand in the current system, fear that the changes MIC is contemplating would open the domestic market to foreign competitors.

¶11. (SBU) At this stage, neither Japan's mobile phone operators nor manufacturers seem to have a working strategy that would enable

them to expand beyond the Japanese market to emerging markets where the real growth potential lies. Instead, they remain locked into a fierce battle for the slow-growing Japanese market using technology that cannot be used in other countries. Mobile phone payment systems or e-money is one of the few areas where Japan now has world-leading services and offers its mobile carriers some real growth potential within Japan.

SCHIEFFER